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OCT 12 1984
ALEXANDER L. STEVAS
CLERK

No. 84-334

IN THE

Supreme Court of the United States

October Term, 1984

PEAT, MARWICK, MITCHELL & CO.,
Petitioner,

—against—

PETER MOSESIAN,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITIONER'S REPLY BRIEF

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PETITIONER'S REPLY BRIEF

Petitioner Peat, Marwick, Mitchell & Co. ("PMM") submits this memorandum in reply to the Brief in Opposition filed by Respondent Peter Mosesian ("Respondent") on October 4, 1984.

I.

THE NINTH CIRCUIT'S DECISION CONFLICTS WITH THE DECISIONS OF THE COURT AND THE DECISIONS OF OTHER COURTS OF APPEAL

Respondent's Brief in Opposition, read together with PMM's Petition, squarely presents the conflict between the standard adopted by the Ninth Circuit in this case for determining the applicability of federal equitable tolling doctrine and the standard enunciated by the Court and applied in other courts of appeal.

PMM—relying upon the Court's decision in *Wood v. Carpenter*, 101 U.S. 135, 141 (1879), and the decisions, *inter alia*, of the First, Second, Seventh and Eighth circuits—has shown in its Petition (pp.

10-13) that a two-step test must be applied. The first analytical step is to determine whether plaintiff is on *notice* of facts sufficient to place him under a duty of inquiry—*i.e.* facts which "excite attention and put a party on his guard and call for inquiry." *Wood v. Carpenter, supra,* 101 U.S. at 141. The second step is whether, *upon diligent inquiry,* plaintiff could have discovered the facts alleged to constitute the breach of legal duty—in the present case, "fraud."

As applied here, the two-step test leads to the following conclusions: (1) the "red flag" events (conceded by Respondent and set forth in the Petition at 8-9) constitute "inquiry notice;" (2) they are sufficient, as a matter of law, to "excite attention and put a party on his guard and call for inquiry" (Petition 13-17); and (3) because Respondent conceded below that he made no inquiry, diligent or otherwise, PMM was entitled, as the district court held, to judgment notwithstanding the verdict.

In his Brief in Opposition, Respondent makes no pretense of having satisfied the two-step test set forth above. Indeed, Respondent openly advocates—and the Ninth Circuit has now adopted —a one-step test. As stated in the opinion below, unless the "red flag" events *"necessarily* suggest *accounting fraud"* (*i.e.* unless they cannot be "explained by . . . events unrelated to accounting fraud"), the statute cannot run as a matter of law (App. C-8) (emphasis added). Consistent with this view, Respondent argues that he is entitled to the benefits of federal equitable tolling doctrine because the "red flag" events did not, on their face, lead *directly and without inquiry* to knowledge of what Respondent alleges were "Peat's improper accounting practices." (Br. in Opp. at 3).*

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* Most accounting "fraud" cases (and the present case is no exception) do not involve "fraud" at all. They merely involve situations in which accountants are alleged to have departed from Generally Accepted Accounting Principles ("GAPP") due to claimed errors of judgment which, at most, constitute simple negligence. Plaintiffs typically characterize such conduct as "recklessness," which, some lower courts have held, supports a claim of "fraud" under the Securities and Exchange Act of 1934 ("1934 Act"). The existence of a claim of "fraud," in turn, bootstraps plaintiffs into an array of procedural advantages conceived to deal with intentionally dishonest conduct.

(footnote continued on page 3)

Obviously, the Ninth Circuit's one-step test completely obliterates any requirement that putative fraud plaintiffs be diligent in determining whether they have claims. Its holding that the statute of limitations cannot run as a matter of law until a plaintiff, *without inquiry*, is confronted with facts which *"necessarily* suggest accounting fraud" squarely conflicts with the rule in several other circuits that it runs, as a matter of law, when plaintiff is on notice that "something is amiss." *Hupp* v. *Gray*, 500 F.2d 993, 996-97 (7th Cir. 1974).*

Respondent next attempts to demonstrate that the Ninth Circuit's holding (that the statute does not run until available facts "necessarily suggest *accounting fraud*") can somehow be harmonized with the Court's decision in *United States* v. *Kubrik*, 444 U.S. 111, 125 (1979), where it was specifically held that the statute does not await the discovery of the *breach of legal duty* ultimately alleged (444 U.S. at 125).

Respondent states: "What distinguishes the present case from *Kubrick* is plaintiff's lack of knowledge of the *cause* of the injury, Peat's *fraudulent* accounting practices. . . ." (Br. in Opp. at 4) (emphasis added). But the whole point of *Kubrick* was to separate discovery of cause in fact from discovery of legal cause (*i.e.* injury stemming from breach of a legal duty) and to establish that the statute runs from discovery of the first and not the second. Respondent now seeks to blur this distinction by arguing—directly contrary to *Kubrick*—that the statute should have been suspended

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(footnote continued from page 2)

One such advantage is "federal equitable tolling doctrine." A requirement that putative plaintiffs "discover," without inquiry, that certain accounting practices do not conform to GAAP is as impractical as a requirement that they discover, without inquiry, whether certain medical treatments conform to proper medical standards (*cf. United States* v. *Kubrick*, 444 U.S. 111 (1979)). Such discovery is not difficult because of concealment (as is the case with fraud). It is difficult because it involves a field of technical professional expertise. To dispose of an inquiry requirement in either case is, in effect, to suspend the statute virtually forever.

* *See also Cook* v. *Avien, Inc.*, 573 F.2d 685, 695-96 (1st Cir. 1978); *Buder* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 644 F.2d 690, 693 (8th Cir. 1981); *Arneil* v. *Ramsey*, 550 F.2d 774, 781 (2d Cir. 1977).

until Respondent discovered PMM's alleged "fraudulent accounting practices"—*i.e.* its alleged breach of legal duty.

Respondent finally argues (Br. in Opp. at 4-5) that a number of other Ninth Circuit cases hold that there is no duty of diligent inquiry and that the statute awaits the discovery of the breach of legal duty alleged. PMM agrees that the Ninth Circuit has generally adopted a federal equitable tolling standard which is inconsistent with *Kubrick* and *Wood* as well as the standard applied in other courts of appeal.*

In conclusion, the one-step test advocated by Respondents and upheld by the Ninth Circuit conflicts with the decisions of other courts of appeal; it is contrary to the law as enunciated by the Court in *Wood* v. *Carpenter* and *United States* v. *Kubrick;* and, as PMM demonstrated in its Petition (pp. 17-19), it leads to injustice and defeats the important policies underlying statutes of limitation without in any way deterring fraud.

I I.

THE SEVENTH AMENDMENT DOES NOT "PRESERVE" ANY RIGHT TO A JURY TRIAL ON THE APPLICABILITY OF FEDERAL EQUITABLE TOLLING DOCTRINE

Respondent, although conceding that federal equitable tolling doctrine "may have equitable origins" (Br. in Opp. at 8), argues that the Court should nonetheless conclude that the Seventh Amendment "preserves" a right to a jury trial on tolling issues (1) because of the "intensely factual nature of the inquiry involved" (*id.* at 7) and (2) because "an unbroken line of precedent from other Circuits" has treated tolling questions as questions for the jury (*id.* at 6). Neither of these arguments withstands analysis.

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* Respondent's suggestion that *Cook* v. *Avien, Inc.*, 573 F.2d 685 (1st Cir. 1978), follows the Ninth Circuit's standard is simply wrong, as a review of that opinion demonstrates. Although it is true that the First Circuit there refers to discovery of the "fraud," the decision makes it plain that inquiry notice was there held to have arisen on the basis of circumstances virtually identical to those in this case.

The remaining cases cited by Respondent from circuits other than the Ninth Circuit (Br. in Opp. at 5) are either consistent (on their facts) with PMM's position here or serve to demonstrate the very confusion and conflict which the Court should resolve.

First, contrary to Respondent's suggestion, there is no such thing as a "jury type" issue (J. Moore, *Federal Practice*, ¶ 38.16[4] at 38-154, ¶ 38.17 at 38-155 to 38-158 (1984)). A plaintiff seeking damages on an issue is generally entitled to a jury trial; a plaintiff seeking an injunction on the same issue must try his case to the court. Thus, as the Court has repeatedly held, the controlling question, in determining whether the Seventh Amendment "preserves" a right to a jury trial with respect to a particular issue is whether that issue was deemed legal or equitable in 1791, when the Seventh Amendment was enacted. Respondent does not (and cannot) contend that tolling issues were not deemed equitable in 1791. They clearly were (Petition at 19-23). Accordingly, the supposedly "intensely factual" nature of tolling issues does not confer any Seventh Amendment right on Respondent.

Nor can the courts of appeal—however unanimous—re-write history or create a Seventh Amendment right where none exists. PMM is aware of only one decision, *State of Ohio* v. *Peterson, Lowry, Rall, Barber & Ross*, 651 F.2d 687 (10th Cir.), *cert. denied*, 454 U.S. 895 (1981), in which a federal court of appeals has even indirectly given any consideration to the historical questions relevant to Seventh Amendment analysis.* Otherwise, certain lower federal courts appear to have uncritically assumed that tolling issues should be assigned to the jury where a jury is the trier of fact.

Nonetheless, the unalterable fact (as shown in the Petition at 19-23) is that, in 1791, an otherwise time-barred litigant could obtain a tolling of the statute of limitations only in a court of equity. Respondent does not contend that this is incorrect. It follows that the Seventh Amendment does not "preserve" any jury trial right with

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* There, the Tenth Circuit recited some of the historical background set forth in the Petition (pp. 20-21) and concluded that the doctrine was indeed an equitable one. The precise question before the court, however, was the proper scope of the lower court's discretion in granting summary judgment on tolling issues; the question of whether a jury trial is ever appropriate on such issues does not appear to have been posed. The court concluded that the equitable origins of tolling doctrine supported a more expansive view of the district court's discretion in granting summary judgment on statute of limitations grounds where tolling has been asserted (651 F.2d at 692-93).

respect to tolling issues and that PMM was entitled to a non-jury trial on those issues in the bifurcated trial below.*

III.

THE LIMITATIONS PERIOD SET FORTH IN SECTION 18(c) OF THE 1934 ACT SHOULD GOVERN CIVIL ACTIONS ARISING UNDER SECTION 10(b)

In its Petition, PMM argued (1) that the current practice in the federal courts of applying "analogous" state statutes of limitation in actions arising under Section 10(b) of the 1934 Act (15 U.S.C. § 78j(b)) encourages forum shopping, securities speculation and tactical delay; (2) that every objective commentator to consider the question has deplored this situation and argued for an analogy to the limitations provisions of the 1934 Act instead; (3) that many courts, although bound by precedent, have expressed the same view; and (4) that the Court has, fairly recently, recognized that the borrowing of analogous federal statutes of limitation is preferable when such an analogy serves to advance federal policies (Petition at 25-27).

Respondent now trivializes the legitimate and widely recognized concerns raised in the Petition, argues that Congress is the proper entity to create a statute of limitations to govern a judicially-created remedy, and concludes that, however unfortunate the consequences, things should stay the way they are now because they have always been that way (Br. in Opp. at 9-11).

Merely to state these arguments is to reject them. However, for the sake of clarity, the following points are worth noting.

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* Rule 38(a) of the Federal Rules of Civil Procedure provides for jury trial as of right only where the Seventh Amendment or some federal statute provides for such a right. Where, as here, no right to a jury trial exists, a jury can render a binding verdict only "with the consent of both parties." Fed. R. Civ. P. 39(c). Since PMM did not so consent (and, indeed, has consistently contested the propriety of a jury trial on tolling issues), the jury's verdict could not have been binding on the district court. *See Armco, Inc.* v. *Armco Burglar Alarm Co., Inc.*, 693 F.2d 1155, 1158 (5th Cir. 1982); *Morelock* v. *NCR Corp.*, 546 F.2d 682, 689 (6th Cir. 1976), *vacated on different grounds*, 435 U.S. 911 (1978); *Hyde Properties* v. *McCoy*, 507 F.2d 301, 306 (6th Cir. 1974); *Cargill, Inc.* v. *Commodity Credit Corp.*, 275 F.2d 745 (2d. Cir. 1960); *Hurwitz* v. *Hurwitz*, 136 F.2d 796, 799 (D.C. Cir. 1943).

First, the essence of PMM's argument is not (as Respondent suggests) that "state limitations periods . . . are *too long*" (Br. in Opp. at 10) (emphasis in original); it is that those limitations periods are *too inconsistent*. This inconsistency, particularly when coupled with completely open-ended tolling doctrines, encourages forum shopping and makes it impossible for companies transacting business nationally to predict when, if ever, their exposure to federal securities fraud liability in connection with a given transaction has ended.

Second, contrary to Respondent's suggestion, nothing in PMM's Petition is inconsistent with "the strong public policy in favor of private enforcement of the federal securities laws" (Br. in Opp. at 9). PMM does not advocate repeal of the federal securities laws. It merely seeks greater predictability in the selection and application of the statutes of limitation governing those laws.

Third, the limitations period set forth in Section 18(c) of the 1934 Act (15 U.S.C. § 78r(c)) is not "specifically inapplicable" to actions arising under Section 10(b) (Br. in Opp. at 9). It is as available for "borrowing" by analogy as any state statute, and, indeed, if logic and policy are a guide, it is far more appropriately available. L. Loss, *Securities Regulation* at 3899-3900 (1969 Supp.).

Finally, the fact that the Court has "noted without criticism" (Br. in Opp. at 9) the current practice of the lower federal courts in this area does not suggest approval or insulate that practice from challenge here.

In short, Respondent simply argues that things should stay the way they are because they are that way. Here, strong policy reasons argue for change. PMM submits that the time for change has arrived.

CONCLUSION

For the reasons stated above and in the Petition, certiorari should be granted.

October 12, 1984

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